FILE COPY

Office - Supreme Court, U. S.
FILED
OCT 13 1939
CHARLES ELMORE CROPLEY
CLERK

Supreme Court of the United States

OCTOBER TERM, 1939.

No. 17.

FORD MOTOR COMPANY, *Petitioner*,

vs.

TOM L. BEAUCHAMP, Secretary of State of the State of Texas, Et Al., *Respondents*.

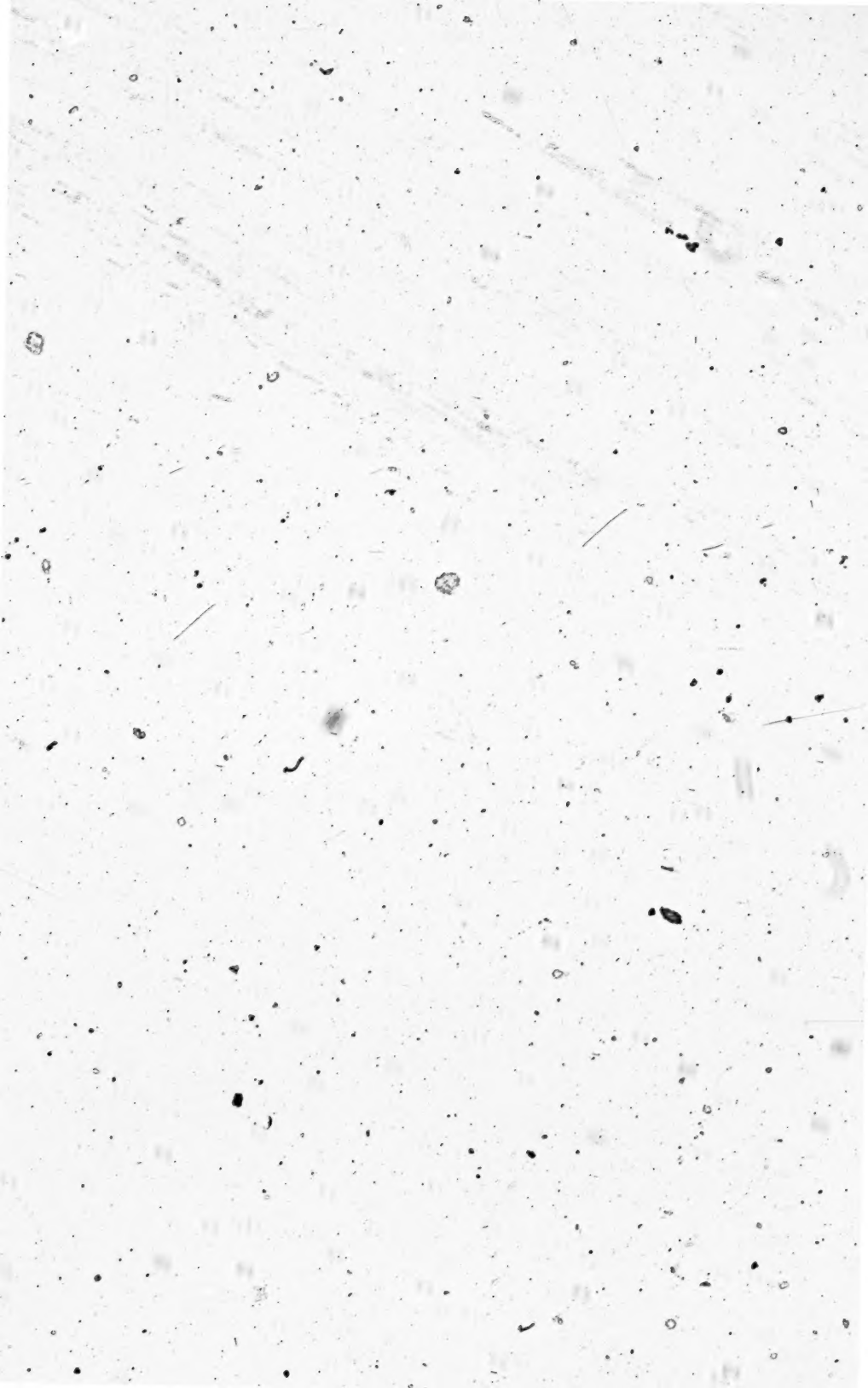
REPLY BRIEF OF PETITIONER.

GAIUS G. GANNON,
Counsel for Petitioner.

PRESS OF BYRON S. ADAMS, WASHINGTON, D. C.

INDEX.

CASES CITED.



Supreme Court of the United States

OCTOBER TERM, 1939.

No. 17.

FORD MOTOR COMPANY, *Petitioner*,

vs.

TOM L. BEAUCHAMP, Secretary of State of the State of Texas, Et Al., *Respondents*.

REPLY BRIEF OF PETITIONER.

Petitioner's position has been fully though concisely stated in the petition for certiorari and in its supporting brief. There will be no attempt to enlarge upon it in this reply, except to the extent that what is said in Respondents' brief is thought to require specific statement from petitioner.

1. Inaccuracies in Respondents' Brief.

(a) Respondents at page 6 of their brief say: "Petitioner enclosed with its report to the Secretary of State its certified check for $1,224.00, which it asserted was the amount it owed as its franchise tax for the year 1936, and

which amount was arrived at by multiplying 3.858000 per cent of the total of all of its business done during the year 1935 into the amount of its capital which was invested by it in the State of Texas, that is, into $3,079,417.96. (See Paragraph 18 of Plaintiff's Petition, Tr. p. 8.)" Respondents labor under a misapprehension of the allegations of Section XVIII of the petition. It is clearly alleged in that section (R. 10, L. 11) "the sum of $1,224.00 which was heretofore paid you is the amount of our franchise tax computed on said figure of $3,079,417.96 * * *." It is thus seen that petitioner's unprotested payment was based on the full book value of all of its property located in Texas. In other parts of the petition it is fully alleged that this property represents all of petitioner's property either located or held in Texas or used by it in connection with Texas operations.

(b) The word "nor" appearing at page 8 of Respondents' brief in the quotation from Section XXII of the petition is in error. The word actually used in the petition is "for". We point this out as the substitution of the word "nor" for the word "for" leaves the quoted allegation unintelligible.

(c) On page 9 of Respondents' brief it is said "there is no allegation in the plaintiff's petition that $34,272,887.72 gross receipts from plaintiff's business done in Texas for the year in question was in any part derived from other than intra-state business."

If by this Respondents assume there is no allegation to show that the $34,272,887.72 gross receipts realized from intra-state sales are not in part attributable to property and activities conducted by petitioner beyond the state then Respondents are clearly in error.

Every fact which can possibly throw any light upon petitioner's total situation in regard to its intra and extra state activities is plead in detail. The way and manner in which the business is conducted is shown. It is alleged that petitioner's Texas business consists exclusively in the assembly and sale of self propelled motor vehicles and parts therefor.

The situs of manufacture and assembly as well as the situs of sale of these self-propelled motor vehicles and parts therefor is plead in detail as is also the value and situs of all of appellants property which is used in connection with its unitary activity. It is shown (R. 20A) that petitioner's capital investment falls in fifteen separate classifications but that in the conduct of its Texas business there is neither located in Texas nor used in or devoted to its Texas operations capital falling in eight of those classifications. The value of petitioner's total capital not used in or in connection with its Texas operations may be arrived at from what is plead by deducting the actual net book value of its actual assets in Texas from the sum total $681,549,928.71 which is plead as the net book value of petitioner's total assets. In the light of the facts as plead it is claimed that the tax demanded "is a tax upon property of ours neither located nor used within the State of Texas and is a tax upon our business transacted outside of the State of Texas." See petitioner's letter of protest to the Secretary of State (R. 19) in connection with the allegation in Section XXIV of the petition (R. 14) that the facts and figures claimed by plaintiff to exist with respect to it and its business in said letter of protest do all and singular in truth and in fact exist as set out in said letter and as shown by the accompanying Exhibit A (R. 20A) attached thereto.

2. The Legislative Scheme of Taxation.

Petitioner has heretofore cited *Investment Securities Co. v. Meharg*, 115 Texas 441, where the Supreme Court of Texas said of the tax under consideration "thus the franchise tax levied on such corporations must have for its basis total gross assets employed by the corporation in the transactions of its business in Texas." Respondents cite *United North and South Development Co. v. Heath, Secretary of State*, 78 S. W. 2d 650, Austin Court of Civil Appeals, writ of error refused. It is not thought that the opinion of the Austin Court is in conflict with that of the Supreme

Court in *Investment Securities Co.* v. *Meharg.* In the Heath case it is said "since such tax is payable in advance the State may in computing such tax, look to the property owned by the corporation and available to it, for use during the ensuing year in carrying on the business. Such was clearly we think the legislative intent." All of the property of the corporation involved in the *Heath* case, as was true of that involved in *Investment Securities Co. of Texas* v. *Meharg*, was located within the State of Texas. It is thought that both courts construe the tax as one measurable solely by capital about to be employed in the prosecution of the local business.

The apportionment formula first came into the statute by an amendment in 1917. It was occasioned by the attack made upon the old law in *Looney* v. *Crane Co.*, 245 U. S. 178. The amendment provided in terms that the fees should be calculated and based upon "capital stock assignable to the Texas business," as allocated by the statutory formula. The amendment of 1917 was incorporated practically in haec verba in the codification of 1925. The present law which is an amendment of the 1925 Code changes the statutory language slightly but only in the interest of brevity and not in a way to indicate any change in legislative intent in regard to the measure of the tax which is still "based upon that portion of the outstanding capital stock, surplus and undivided profits * * *."

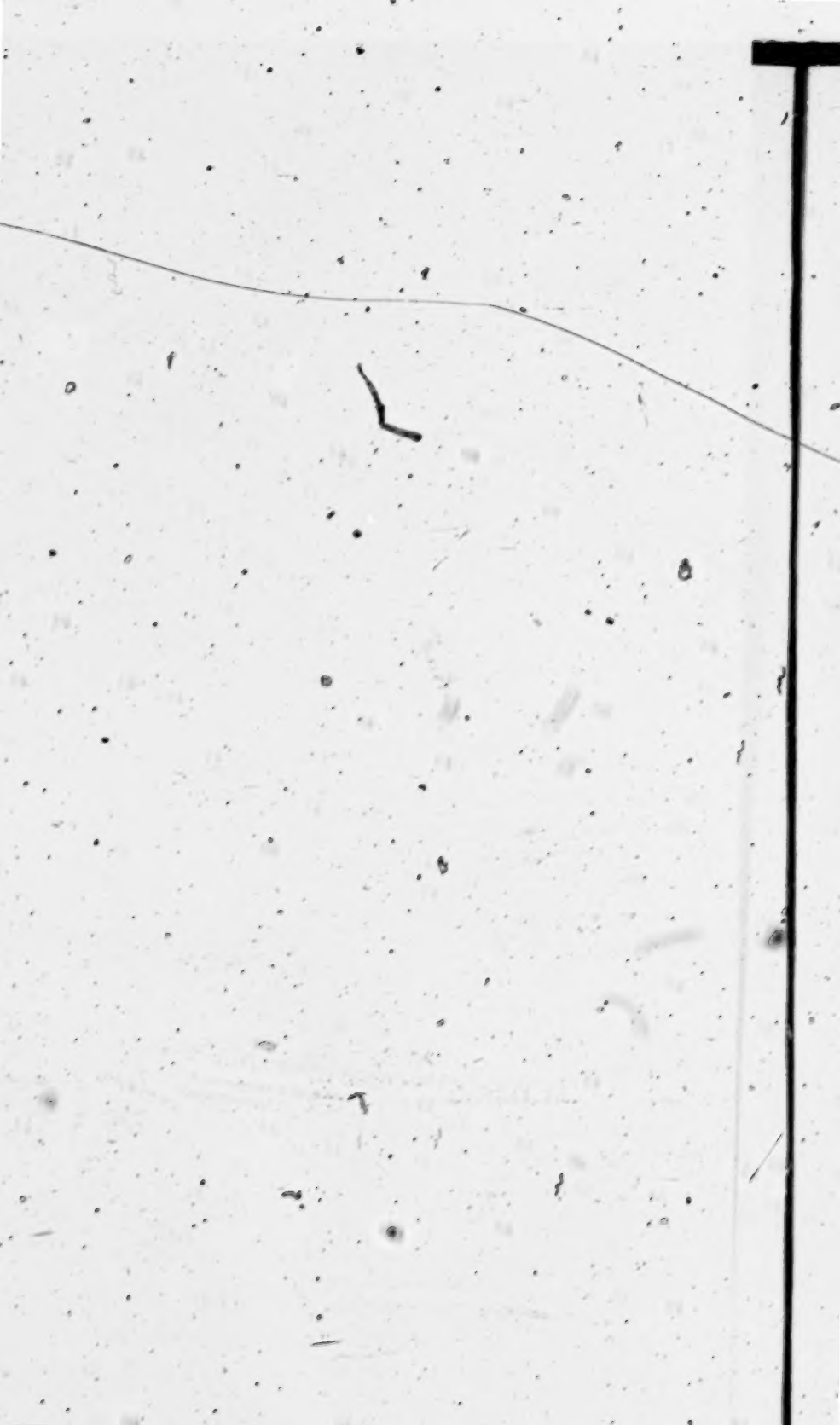
Though at one point in their brief Respondents seemed to agree that the measure of the tax is solely capital about to be employed in the prosecution of the local business (page 23 *et seq.*) still at another point in their brief they say the statute "bears inherent evidence that it was carefully and intelligently conceived, so as to bear equally as nearly as possible upon all corporations according to the value of their *business potency* while exercising the privilege of carrying on the business within the state."

In the light of *Investment Securities Company of Texas* v. *Meharg* it is submitted that total business potency in the

Allocation to Texas
Of Capital and Surplus by Ratio of Gross Receipts
Under Varying Conditions

	Total Gross Receipts Entire Company (Col. 1)	Gross Receipts In Texas (Col. 2)	Ratio of Gross Receipts in Texas to Total Gross Receipts (Col. 3)	CAPITAL AND SURPLUS ALLOCATED TO TEXAS BY GROSS RECEIPTS: When Capital and Surplus Is $200,000,000 (Col. 4)	When Capital and Surplus Is $400,000,000 (Col. 5)	When Capital and Surplus Is $600,242,151 (Col. 6)	When Capital and Surplus Is $800,000,000 (Col. 7)
Corporation L	$ 400,000,000.00	$ 7,716,121.20	.019290303	$ 3,858,060.60	$ 7,716,121.20	$11,578,852.98	$15,432,242.40
Corporation M	800,000,000.00	15,432,242.40	.019290303	3,858,060.60	7,716,121.20	11,578,852.98	15,432,242.40
Corporation N	1,200,000,000.00	23,148,363.60	.019290303	3,858,060.60	7,716,121.20	11,578,852.98	15,432,242.40
Corporation O	1,776,689,950.94	34,272,887.72	.019290303	3,858,060.60	7,716,121.20	11,578,852.98	15,432,242.40
Corporation P	2,000,000,000.00	38,580,606.00	.019290303	3,858,060.60	7,716,121.20	11,578,852.98	15,432,242.40
Corporation Q	200,000,000.00	7,716,121.20	.038580606	7,716,121.20	14,432,242.40	23,157,705.95	30,864,484.80
Corporation R	400,000,000.00	15,432,242.40	.038580606	7,716,121.20	14,432,242.40	23,157,705.95	30,864,484.80
Corporation S	600,000,000.00	23,148,363.60	.038580606	7,716,121.20	14,432,242.40	23,157,705.95	30,864,484.80
Corporation T	888,344,975.47	34,272,887.72	.038580606	7,716,121.20	14,432,242.40	23,157,705.95	30,864,484.80
Corporation U	1,000,000,000.00	38,580,606.00	.038580606	7,716,121.20	14,432,242.40	23,157,705.95	30,864,484.80
Corporation V	133,333,333.34	7,716,121.20	.057870909	11,574,181.80	23,148,363.60	34,736,558.93	46,296,727.20
Corporation W	266,666,666.67	15,432,242.40	.057870909	11,574,181.80	23,148,363.60	34,736,558.93	46,296,727.20
Corporation X	400,000,000.00	23,148,363.60	.057870909	11,574,181.80	23,148,363.60	34,736,558.93	46,296,727.20
Corporation Y	592,229,983.65	34,272,887.72	.057870909	11,574,181.80	23,148,363.60	34,736,558.93	46,296,727.20
Corporation Z	666,666,666.67	38,580,606.00	.057870909	11,574,181.80	23,148,363.60	34,736,558.93	46,296,727.20

2-26-37



sense that term is used in such cases as *Atlantic Refining Co.* v. *Virginia*, 302 U. S. 22, is in no proper sense a factor in the legislative scheme of taxation.

The measure of the tax is either capital about to be employed in Texas business, or gross receipts from intra-state sales or services, or some inscrutible combination of the two. Viewed as a tax measured otherwise than by capital alone the statute, in practical operation, reaches strange results. We append at this point a table of computations to show allocations to Texas of capital and surplus by the single factor of ratio of gross receipts under varying conditions. From this table it is readily seen that the tax is not increased in direct relation to the volume of intra-state receipts but that it is solely dependent upon the *ratio* of intra-state receipts to total receipts. Thus, a corporation with total capital and surplus of $200,000,000, doing business both in and out of the state; has allocated to Texas of its total capital $3,858,060.60 when gross receipts from Texas amount to $7,716,121.20, total gross receipts amounting to $400,000,000, the ratio being .019290303. The same corporation may increase its Texas receipts by five fold to $38,580,606 without increase in allocation of capital to Texas provided only that at the same time it increases its total sales to $2,000,000,000 so as to preserve the ratio of .019290303. Thus, the Texas tax is the same in the case of a business whose Texas gross receipts are in excess of $38,000,000 as in the case of a business whose Texas gross receipts are under $8,000,000, provided only that extra-state and inter-state gross receipts are increased in proportion.

It is submitted that reasonably construed the statute cannot be viewed as measuring the tax in relation to the amount of Texas sales, as the statutory formula, in practical operation, produces an increase or decrease in capital allocable to Texas not on a corresponding increase or decrease in Texas receipts but solely in relation to the *ratio* of those receipts to total gross receipts from all business

wherever done. We assume without discussion that the *ratio* in itself is unimportant and may not be said to relate, even remotely to the value of the taxed privilege.

Respondents' contentions therefore we think must be examined in the light of a tax whose incidence is on a privilege but which values that privilege solely in relation to capital about to be employed in its exercise.

3. Respondents' Second Counter Proposition to Petitioner's Specifications of Error.

By this counter proposition respondents frankly admit that the result of the Texas statute in its application to petitioner is to measure the value of a purely intra-state privilege in relation to capital employed and activities conducted by petitioner beyond the confines of the State. Respondents would justify this sweep of the statute on the grounds that this extra-state property and these extra-state activities are considered only to the extent that they enhance the value of what is done in Texas. But under the allegation of the petition what is done or used without the state adds nothing to the value of what is done within. It seems to us that respondents follow the Circuit Court of Appeals in an argument which has been repudiated by this Court in *Hans Rees' Sons* v. *North Carolina*, 283 U. S. 123.

In that case the Supreme Court of North Carolina had ruled in respect to corporations conducting a unitary business in several states that any of the states were justified as viewing what was done within its borders as "the hub from which the spokes of the entire wheel radiate to the outer rim" and in refusing to lop off as foreign to it "certain elements of the business constituting a single unit in order to place the income beyond the taxing jurisdiction of this state." The following language from this Court's opinion on appeal from the judgment of the Supreme Court of North Carolina is directly applicable:

> "Undoubtedly, the enterprise of a corporation which manufactures and sells its manufactured product is

ordinarily a unitary business, and all the factors in that enterprise are essential to the realization of profits. The difficulty of making an exact apportionment is apparent and hence, when the State has adopted a method not intrinsically arbitrary, it will be sustained until proof is offered of an unreasonable and arbitrary application in particular cases. But the fact that the corporate enterprise is a unitary one, in the sense that the ultimate gain is derived from the entire business, does not mean that for the purpose of taxation the activities which are conducted in different jurisdictions are to be regarded as 'component parts of a single unit' so that the entire net income may be taxed in one State regardless of the extent to which it may be derived from the conduct of the enterprise in another State. As was said in the *Bass* case with regard to 'the unitary business of manufacturing and selling ale' which began with manufacturing in England and ended in sales in New York, that State 'was justified in attributing to New York its proportion of the profits earned by the Company from such unitary business'. And the principle that was recognized in *National Leather Co.* v. *Massachusetts, supra,* was that a tax could lawfully be imposed upon a foreign corporation with respect to 'the proportionate part of its total net income which is attributable to the business carried on within the State.' When, as in this case, there are different taxing jurisdictions, each competent to lay a tax with respect to what lies within, and is done within, its own borders, and the question is necessarily one of apportionment, evidence may always be received which tends to show that a State has applied a method, which, albeit fair on its face, operates so as to reach profits which are in no just sense attributable to transactions within its jurisdiction."

It was said in *Wallace* v. *Hines,* 253 U. S. 66, that a state when establishing tax values is justified in looking to activities and property beyond its borders only when those activities and that property may be seen to add in a clear and unmistakable way to the value of what lies or is done within. We have heretofore pointed out that the result of the Texas

formula which considers only "gross receipts" from business done as distinguished from "business done" is to apportion to Texas pro tanto *the whole* of petitioner's unitary activity resulting in intra-state sales. Compare *James* v. *Dravo Contracting Co.*, 302 U. S. 134. Even if the legislative scheme of taxation were—as it is not—to allocate, in part, to Texas out of state property, thought to be remotely and indirectly related to Texas activity, on the theory that that property adds, in some degree, to the value of the local privilege, still in any event an apportionment is required. Otherwise, all extra-state activity entering into the unitary scheme is denied effect. But the statute permits of no apportionment. Petitioner may not by valuing its extra-state activities, say in relation to net income, bring this value within the framework of a statute which allocates property solely on the basis of gross receipts.

If it is to be said that the Texas Act evidences an intention to value the local privilege, in part in relation to the amount of business done in Texas, as distinguished from capital employed in the business, then it seems to us it must be said with equal logic of the statute reviewed in *Wallace* v. *Hines*, 253 U. S. 66, that the legislative scheme there was to value the local privilege in relation, in part, to the number of miles of railway operated within the state. But no such suggestion was brought forward in the *North Dakota* case. It is submitted that, as was true of the factor of miles of railway operated within the State in the North Dakota statute, the sole function to the purposes of the Texas Act, of the factor of gross receipts from Texas business is to arrive at the amount of property employed in Texas business. If this view be correct then under the principles announced in this Court's prior cases, *Western Union* v. *Kansas*, 216 U. S. 1, *Looney* v. *Crane*, 245 U. S. 178, the effect of the Texas Act on petitioner is to subject petitioner's property beyond the confines of the state to unconstitutional taxation. Texas in looking beyond its borders to petitioner's Michigan manufacturing activity and

in allocating to itself all of the property there situated, to the extent that its use results in Texas sales, goes too far. In *Great Atlantic and Pacific Tea Co.* v. *Grosjean*, 301 U. S. 412, extra-state capital and activities where permitted to be considered in valuing a local privilege but only to the extent as shown by the record in that case this extra-state property and activity added to the value of the local privilege. There is no room on the facts plead here for the application of the *Grosjean* case.

4. Respondents' Authorities.

In the interest of brevity we will notice only a few of the authorities cited by respondent.

Southern Realty Corporation, et al. v. *McCallum*, 65 Fed. 2d 934.

It is respectfully submitted that in the *McCallum* case the statute now in question was not attacked upon the same ground on which petitioner stands. It would serve no useful purpose to review the decision in detail. However, what was actually decided is manifest from the concluding part of the opinion where it is said: "It is true that a taxing statute may be valid in its general application, but unconstitutional in its operation on some particular person and evidence is receivable to show it. *Hans Rees' Sons* v. *North Carolina, Ex. Rel. Maxwell*, 283 U. S. 124, 51 S. Ct. 385, 75 L. Ed. 879. No such showing has in our judgment been made here." The *McCallum* case is not authority for the proposition that the statute under review is immune to attack in a proper case. On the contrary it appears to support the opposite view.

People Ex. Rel. v. *Bass*, 266 U. S. 271;
Underwood Typewriter Co. v. *Chamberlain*, 254 U. S. 113.

In view of what was said of these cases in *Hans Rees' Sons* v. *North Carolina*, *supra*, it is thought they have no

application here where it is unequivocally alleged that Texas allocates to itself *all* of the property used by petitioner in its unitary activities conducted in several states to the extent that those activities ultimately result in Texas sales.

International Shoe Company v. *Shartell*, 279 U. S. 429;
New York v. *Latrobe*, 279 U. S. 421.

As we read these companion cases they announce nothing in addition to what was decided in *Roberts and Schaefer Co.* v. *Emerson*, 271 U. S. 51. In all three cases the question was the right of the state to value non-par stock arbitrarily for franchise tax purposes. None of them involve a question of unjust and unreasonable apportionment which as we see it is the only thing at issue in the present case. We, therefore, are at a loss to understand respondent's statement at page 37 of their brief that "the Latrobe case negatives every proposition urged by petitioner against the Texas statute."

5. Respondents' Contention that Because the Amount of the Tax is Small in Relation to the Privilege Granted Petitioner Has No Standing to Complain.

Respondents urged in the Circuit Court with much effect the contention that as the amount of the tax was equivalent to only two ten-thousandths of one per cent (.0002%) of petitioner's gross receipts for the year in question the statute is not subject to attack. But there is no support in the decisions of this court for the view that an unconstitutional *method* of taxation will be allowed to stand because the *amount* of the tax is small. This is not a case where the results under the statute *approach* actuality. Here Texas allocates to itself approximately eight times as much capital as is actually used by petitioner in its Texas business. If what respondents really say is that de minimis applies,

then the answer is to be found in the statement of this court in *Alpha Portland Cement Company* v. *Massachusetts*, 268 U. S. 203, quoted with approval in *Cudahy Packing Co.* v. *Hinkle*, 278 U. S. 460, where it was said of state taxes found to burden inter-state commerce and to violate the 14th Amendment because beyond the jurisdiction of the state to levy, that "the *amount* demanded is unimportant when there is no legitimate *basis* for the tax."

CONCLUSION.

In conclusion it is respectfully submitted that as applied to petitioner the tax in question works unconstitutional results.

Respectfully submitted,

GAIUS G. GANNON,
Counsel for Petitioner.